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No. 82-155

In the Supreme Court of the United States

OCTOBER TERM, 1982

CREDITHRIFT OF AMERICA, INC., PETITIONER

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

MEMORANDUM FOR THE UNITED STATES IN OPPOSITION

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Petitioner contends that application of the lien avoidance provision of the Bankruptcy Reform Act of 1978, 11 U.S.C. (Supp. IV) 522(f)(2), to liens acquired after enactment of the statute but before its effective date is unconstitutional.

1. The Bankruptcy Reform Act of 1978, Pub. L. No. 95-598, 92 Stat. 2549, 11 U.S.C. (Supp. IV) 101 *et seq.*, was enacted in November 1978 and became effective on October 1, 1979. Under the Act, a debtor may "avoid the fixing of a lien * * * to the extent that such lien impairs an exemption * * * if such lien is * * * a nonpossessory, nonpurchase-money security interest in * * * household furnishings, household goods, * * * [or] appliances * * *." 11 U.S.C. (Supp. IV) 522(f)(2).

On July 2, 1979, petitioner made a loan to Everett and Elizabeth Yoder, receiving in return a note for $2,508.90 and a signed form in which the Yoders pledged their household furnishings, goods, and appliances as security for the

loan (Pet. App. 7-8). On July 23, 1979, petitioner made a similar loan to Harry and Susan Marie Webber, receiving in return a note for $3,224.96 and a similar security agreement (*id.* at 8). The parties stipulated that both liens were nonpossessory, nonpurchase-money security interests acquired during the period between the enactment of the Bankruptcy Reform Act and its effective date (*ibid.*).

Subsequent to the effective date of the Bankruptcy Reform Act, the Yoders and the Webbers filed petitions in bankruptcy (Pet. App. 8). Pursuant to Section 522(f)(2), each couple sought to avoid petitioner's liens on their exempt household property (*ibid.*). In response, petitioner asserted that Section 522(f)(2) cannot constitutionally be applied to liens arising during the "gap" between the enactment and the effective date of the Act. Pursuant to 28 U.S.C. 2403(a), the United States intervened in the bankruptcy court to defend the constitutionality of Section 522(f)(2) as applied in these cases (Pet. App. 8-9).

The bankruptcy court held that there is no constitutional barrier to the avoidance of such "gap" liens under Section 522(f)(2) (Pet. Supp. App. 36-60). The court reasoned that permitting debtors to avoid "gap" liens was not a retrospective application of Section 522(f)(2) at all; any effect on liens created after the Act's enactment was a *prospective* effect of the statute (Pet. App. 48-49). Assuming arguendo that the application of Section 522(f)(2) here could be characterized as retrospective, the bankruptcy court concluded that it was not so "unreasonable, arbitrary, capricious, or unfair" (Pet. App. 51) as to violate the Fifth Amendment.

The court of appeals affirmed (Pet. App. 1-31; 674 F. 2d 796 (1982)). After noting the flood of litigation involving the constitutionality of retrospective application of Section 522(f)(2) (see Pet. App. 11-16), the court of appeals stated that "a close question is presented" by the instant case,

but "agree[d] with the bankruptcy court * * * that it is 'not unreasonable to impute to credit companies * * * the knowledge and understanding of a new law *after* that law has been enacted' " (*id.* at 28-29) (emphasis in original).

In a separate concurrence (Pet. App. 29-31), Judge Schroeder stated that this case "simply does not present a substantial question, much less a close one" (*id.* at 30). She explained (*id.* at 31):

> Congress could have made the Act effective from the date of its passage. Had it done so, application of the exemption provisions to this post-enactment lien would raise no possible question of retroactive interference with property rights. Instead, Congress gave some lead time for the public to gain familiarity with the new Act and to adjust debtor/creditor practice accordingly. The creditor can hardly claim to have been prejudiced by Congressional leniency in deferring the effective date.

2. As petitioner acknowledges (Pet. 11), no other court of appeals has ruled on the constitutionality of Section 522(f) as applied to "gap" liens.[1] The flood of litigation involving the constitutionality of retrospective application of Section 522(f) has involved application of the Section

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[1]The Third and Seventh Circuits clearly agree with the decision below, however, because they have held Section 522(f) constitutional even as applied to pre-enactment liens. *In re Gifford*, No. 81-1174 (7th Cir. Aug. 18, 1982) (en banc); *In re Ashe*, 669 F. 2d 105 (3d Cir. 1982), petition for cert. pending, No. 81-1866 (filed Apr. 6, 1982). The one court of appeals that has held unconstitutional retrospective application of Section 522(f) expressly limited its analysis to liens arising before the enactment of the Bankruptcy Reform Act (see *Rodrock* v. *Security Industrial Bank*, 642 F. 2d 1193, 1196 n.3 (10th Cir. 1981), prob. juris. noted *sub nom. United States* v. *Security Industrial Bank*, No. 81-184 (Dec. 14, 1981)), and that decision in no way suggests that avoidance of a "gap" lien would be unconstitutional. See page 5, *infra*. See also *in re Gifford*, *supra*, slip op. 34 n.6 (Pell. J., dissenting).

to liens arising *before* its enactment. See generally cases cited at Pet. App. 11-16. Thus, there is no conflict in the lower courts on the issue presented here that warrants this Court's attention.

Because petitioner's liens arose after the enactment of the Bankruptcy Reform Act, petitioner's assertion that this case conflicts with *Louisville Joint Stock Land Bank* v. *Radford*, 295 U.S. 555 (1935), is totally without foundation. In *Radford*, the Frazier-Lemke Act of 1934 was held unconstitutional because it deprived mortgagees of rights in specific property that had vested prior to the enactment of the statute. See 295 U.S. at 589, 595. The Court specifically noted, however, that while the legislation at issue in the case was unconstitutional, "[t]he power over property pledged as security after the date of the Act may be greater than over property pledged before." 295 U.S. at 589.

In our view, Judge Schroeder's concurring opinion below is correct; this case presents no substantial constitutional question. Congress could have made the Bankruptcy Reform Act effective immediately upon its enactment. Had it done so, there would be no doubt whatsoever that Section 522(f)(2) could be applied constitutionally to liens created eight months later, such as those involved in this case. Because enactment of the Bankruptcy Reform Act put petitioner on notice that, after the effective date of the Act, nonpossessory, nonpurchase-money security interests in exempt household goods would be subject to avoidance, any security agreements concerning such goods entered into by petitioner after enactment of the Act were subject to this condition. See *Diamond Glue Co.* v. *United States Glue Co.*, 187 U.S. 611, 615 (1903); *Pinney* v. *Nelson*, 183 U.S. 144, 147 (1901). And because petitioner was fully aware when it entered into the security agreements that the liens would be subject to avoidance under Section 522(f)(2) after October 1, 1979, application of the statute to these

liens is not unfair and in no way interferes with any "investment-backed expectation" of petitioner's that would suggest an unconstitutional taking. Cf. *Penn Central Transportation Co.* v. *New York City*, 438 U.S. 104, 124 (1978).

For the foregoing reasons, we do not agree with petitioner (Pet. 13) that this case is "similar" to *United States* v. *Security Industrial Bank*, No. 81-184, which is now pending before this Court. That case involves the constitutionality of Section 522(f)(2) as applied to nonpossessory, non-purchase-money liens acquired *before* enactment of the Bankruptcy Reform Act. As explained in our brief in that case, we contend that Section 522(f)(2) is constitutional as applied to such pre-enactment liens. But even if our view is rejected and the judgment in *Security Industrial Bank* is affirmed, the decision below would not be called into question because petitioner acquired its liens with full knowledge, and subject to the condition, that they might be avoided in bankruptcy under Section 522(f)(2) after October 1, 1979. Accordingly, it is unnecessary to hold the petition in this case pending the disposition of *United States* v. *Security Industrial Bank, supra.*

It is therefore respectfully submitted that the petition for a writ of certiorari should be denied.

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Solicitor General

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